amount attributable to the conversion features of the bond.

(2) The value of the conversion features of a particular bond shall be ascertained as of the time of acquisition by reference to the assumed price at which such bond would be purchased on the open market if without conversion features, and by subtracting such assumed price from the cost of the bond. The assumed price of the bond without conversion features shall be ascertained by comparison to the yields on which bonds of similar character, not having conversion features, are sold on the open market and adjusting the price of the bond in question to this yield. This adjustment may be made by the use of standard bond tables. In selecting quotations for comparative purposes, bonds of the same classification and grade shall be used.

(3) The application of the principles set forth in this paragraph may be illustrated as follows:

Example. T purchased for $115 a $100 bond, maturing in 10 years, on which interest is payable semiannually at the rate of 3 percent a year. This bond is convertible into common stock at the option of the holder. It is found that bonds of the same character, not having conversion features, were sold on the open market on or about the time of T's purchase on a basis to yield 2.6 percent. By recourse to a standard bond table, it is found that the cost of a 3 percent, 10-year, $100 bond to yield 2.6 percent would have been $103.50. Since the taxpayer paid $115 for the convertible bond, the difference between $115 and $103.50, or $11.50, represents the value of the conversion features of the bond at the time of purchase. The balance of $3.50 represents the bond premium subject to amortization under section 171.

(4) If a convertible bond acquired on or before June 15, 1950, is held during the taxable year, the amortizable bond premium shall be computed as if the provisions for the determination of the bond premium without the inclusion of any amount attributable to the conversion features of the bond were applicable for each year for which the bond was held prior to such taxable year. Thus, if T, in the example in subparagraph (3) of this paragraph, had acquired the bond on January 1, 1949, and if T makes his income tax returns on the basis of the calendar year, the amortizable bond premium for 1957 would be $0.35, determined as follows:

Bond premium not attributable to conversion feature	$3.50
Amortizable bond premium for 1949 and 1950, determined by reference to bond premium not attributable to conversion feature	.70
Portion of bond premium amortizable over remaining life of bond	2.80
Amortizable bond premium for each of the remaining 8 years, including the taxable year 1957 (one-eighth of $2.80)	.35

(d) *Capitalized expenses.* (1) In the case of a bond to which section 171 otherwise applies, on which the bond premium is attributable only to capitalized expenses (such as buying commissions), if a taxpayer:

(i) Regularly employs a reasonable method of amortization under which capitalized expenses are amortized, or

(ii) Is required by the regulations to use the method of amortization prescribed by paragraph (f) of this section, or

(iii) Regularly employs a reasonable method of amortization but does not amortize capitalized expenses, such taxpayer is permitted, but is not required, to amortize capitalized expenses in accordance with such method.

(2) In the case of a bond to which section 171 applies and on which there is bond premium exclusive of capitalized expenses:

(i) If a taxpayer regularly employs a reasonable method of amortization under which capitalized expenses are treated as being part of the bond premium for purposes of amortization, such capitalized expenses must be treated as being a part of the bond premium for the purposes of section 171.

(ii) If a taxpayer is required by regulations to use the method of amortization prescribed by paragraph (f) of this section, he must treat capitalized expenses as being part of the bond premium for purposes of section 171.

(iii) If a taxpayer regularly employs a method of amortization under which capitalized expenses are not treated as being part of the bond premium for the purposes of amortization, he is permitted, but is not required, to treat such capitalized expenses as being part of the bond premium for the purposes of section 171.

(e) *Taxable years in which interest not received or accruable.* In the case of a taxpayer who makes his income tax returns on the cash receipts and disbursements method or one who makes his returns on an accrual method and who owns a bond to which section 171 applies and in respect of which no interest is received or accrued by the taxpayer during the taxable year, if the taxpayer:

(1) Regularly employs a reasonable method of amortization under which the bond premium on such bond for such taxable year is amortized, or

(2) Is required by the regulations to use the method of amortization prescribed by paragraph (f) of this section, or

(3) Regularly employs a reasonable method of amortization under which the bond premium on such bond for such taxable year is not amortized, such taxpayer is permitted, but not required, to amortize bond premium on the bond for such taxable year in accordance with such method.

(f) *Methods of amortization.* (1) Determination of the bond premium and amortizable bond premium on any bond to which section 171 applies shall be made in accordance with:

(i) The method of amortization regularly employed by the taxpayer, if such method is reasonable; or

(ii) In all other cases, the method of amortization prescribed by this section.

A method of amortization, for example, the composite method described in § 1.1016–9, will be deemed ''regularly employed'' by a taxpayer if the method was consistently followed in taxable years beginning before January 1, 1954, or if for taxable years beginning on or after such date a taxpayer who has never previously taken a deduction for amortization initiates in the first taxable year for which such deduction is taken a reasonable method of amortization and consistently follows such method thereafter. A taxpayer who regularly employs a method of amortization may be one, for example, who is subject to the jurisdiction of a State or Federal regulatory agency and who, for the purposes of such agency, amortizes the bond premium on his bonds in accordance with a method prescribed or approved by such agency. However, it is not necessary that the taxpayer be subject to the jurisdiction of such an agency or that the method be prescribed or approved by such agency. It is sufficient if the taxpayer regularly employs a method of amortization and if such method is reasonable.

(2) The bond premium to be amortized shall be determined under the following method:

(i) The amortizable bond premium on such bond attributable to the taxable year under paragraph (a)(6) of this section shall be an amount which bears the same ratio to the bond premium on the bond as the number of months in the taxable year during which the bond was held by the taxpayer bears to the number of months from the beginning of the taxable year (or, if the bond was acquired in the taxable year, from the date of acquisition) to the date of maturity or earlier call date. For the purposes of this subdivision, a fractional part of a month shall be disregarded unless it amounts to more than half of a month, in which case it shall be considered as a month.

(ii) For purposes of subdivision (i) of this subparagraph, the bond premium as of any date on any bond to which section 171 applies shall be determined in accordance with paragraph (a) of this section by ascertaining the excess of the amount of the basis of the bond, as determined under section 1011 (adjusted to date for amortizable bond premium under section 1016) over the amount payable at maturity or, in the case of a callable bond, the earlier call date (except as otherwise provided in paragraph (a)(2) and (3) of this section).

(3) The application of the provisions of this paragraph relating to method of amortization may be illustrated by the following example:

Example. (i) A taxpayer, who makes calendar year returns on June 20, 1955, acquires at a cost of $119 a $100 bond issued January 1, 1955, maturing January 1, 1965. The amortizable bond premium as of the last day of 1955 is computed as follows:

Bond premium at date of acquisition	$19
Number of months in 1955 during which bond is held by the taxpayer	6
Number of months from date of acquisition to date of maturity	114
Amortizable bond premium (6/114×$19) equals	1